

Expansion of Federal Reserve's TALF to include certain CMBS issued prior to January 1, 2009

The Federal Reserve Bank of New York (the "Fed") recently announced that, beginning in July, funds from the Term Asset-Backed Securities Loan Facility (TALF) may be used to finance the acquisition of certain commercial mortgage-backed securities (CMBS) issued before January 1, 2009. The Fed's goal is that this expansion of TALF will create a market for legacy CMBS and stimulate the extension of new credit by easing balance sheet pressures on banks and other financial institutions currently holding CMBS.

Terms and Conditions of TALF Legacy CMBS Loans

- *Qualifying Securities.* To qualify as legacy CMBS eligible under TALF, each CMBS must meet certain criteria, including issuance before January 1, 2009, a current credit rating in the highest long-term investment-grade rating category from two qualifying rating agencies, and 95% of the principal balance of the CMBS loans must be secured by interests in properties located in the U.S. Also, each CMBS must evidence an interest in a trust fund consisting of fully-funded mortgage loans and generally not other CMBS, other securities or interest rate swap or cap instruments or other hedging instruments, and qualifying legacy CMBS must not have been junior to other securities with claims on the same pool of loans.
- *Voting Rights.* A TALF borrower cannot exercise any voting, consent or waiver rights under a CMBS without the Fed's consent.
- *Loan Amount.* The maximum size of a TALF loan secured by a CMBS will be the current market price of the CMBS minus a required equity contribution from the borrower equal to a minimum of 15% of par. Required equity from borrowers increases by one percentage point of par for each year of average life of the CMBS beyond five years. For example, assuming a CMBS with a par value of 100 and a seven-year weighted average life, with a required equity contribution of 17% of par, then: (i) if the market price is 75% of par, the loan amount is 58 (75-17) and the required equity from the borrower is 23% (17/75) of the purchase price; and (ii) if the market price is 50% of par, the loan amount is 33 (50-17) and the required equity contribution from the borrower is 34% (17/50) of the purchase price.
- *Loan Term and Interest Rates.* The minimum loan amount under TALF generally is \$10 million. Each TALF loan secured by a CMBS will have a three- or five-year maturity at the election of the borrower. Three-year TALF loans will bear interest at a fixed annual rate equal to 100 basis points over the three-year Libor swap rate. Five-year TALF loans will bear interest at a fixed annual rate equal to 100 basis points over the five-year Libor swap rate.
- *Remittance of Principal.* Any remittance of principal on the CMBS must be used immediately to reduce the principal amount of the TALF loan in proportion to the equity contributed by the borrower.
- *Fed Discretion.* The Fed will retain the right to reject any CMBS as TALF loan collateral based on the Fed's risk assessment. In assessing risk, the Fed will engage a collateral monitor and will pay attention to myriad factors to

determine the quality of the underlying CMBS mortgage pool, including anticipated performance of the pool under stress.

- *Terms in General.* In general, the established terms and underwriting requirements of the TALF program are expected to apply to legacy CMBS loans unless specifically stated otherwise.

Additional Information

The initial subscription date for TALF loans collateralized by legacy CMBS will be in late July, 2009. The subscription and settlement cycle for legacy CMBS will occur in the latter part of each month, whereas the cycle for non-CMBS TALF asset classes will remain in the first half of the month.

The Fed announced that it is still working on additional terms and conditions, and therefore the foregoing is subject to change. For example, the Fed may limit the volume of TALF loans secured by legacy CMBS, and is considering whether to allocate such volume through an auction or other procedure, and the Fed may require that TALF loans for legacy CMBS be used to fund recent secondary-market arm's-length transactions. The Fed has promised additional information in advance of the initial subscription date for legacy CMBS.

To read the Federal Reserve Board's press release, as well as the terms and conditions and FAQs relating to the TALF legacy CMBS loan program, please click [here](#).

If you would like further information, please contact one of the attorneys listed below or the Ropes & Gray attorney who usually advises you.

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